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ALEXANDER L. STEVAS,
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IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1980

No.

J. NAT and JENICE HAMRICK,

PETITIONERS

versus

COMMISSIONER OF INTERNAL REVENUE,

RESPONDENT

Petition for a Writ of Certiorari to the United States Court of Appeals for the Fourth Circuit

---

J. Nat Hamrick and
Jenice Hamrick, (Pro Se)

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P. O. Drawer 470
Rutherfordton,
North Carolina 28139

QUESTIONS PRESENTED FOR REVIEW

1. Can a taxpayer be denied credit for the loss of a farm when:

She owned a 1/2 interest in a 936 acre farm and had no funds to buy seed, to buy fertilizer, to pay labor or purchase machinery, and when

The only way she could farm the land was to get a farm oriented corporation in which she held stock to farm it for her;

AND WHEN that corporation could not farm it for her without mortgaging the property to obtain the necessary funds to farm it,

AND WHEN after several bad crop years, the mortgage was foreclosed and the farm lost?

2. Can the tax court establish the value of taxpayer's 1/2 interest in the said property as of the year 1920 at $38,000.00,

WHEN the only people who were familiar with the land in 1920 testified as follows - Walter Frederick Marvin said it was worth at

least $250.00 an acre and another, Winchester Grahm, testified it was worth four times more than surrounding open land, and both based their opinions on the fact that it was a highly cultivated plantation with houses, barns, packing sheds, cotton gin, syrup mill, pecan orchard and a small school on the property,

AND WHEN the only expert witness for the government based his opinion on sales of unimproved open land and testified that he did not take into consideration the improvements, to wit, cotton gin, seed storage warehouse, grain storage warehouse, packing sheds, syrup mill, livestock barn, pecan orchard, asparagus packing house and barn and windmill?

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GROUNDS UPON WHICH THE JURISDICTION OF THIS COURT IS INVOKED ARE:

This Court's opinion is in direct conflict with Jefferson Patterson and Marvin Patterson v. United States, 459 F.2d 487, and Mercer v. Commissioner of Internal Revenue, 376 F.2d 708 (1967) and Fox v. Commissioner of Internal Revenue, 190 F.2d 101 (1951).

(i) The date of the decision of the Tax Court was March 5, 1979, Docket No. 7250-75.

(ii) The date of the decision of the United States Court of Appeals for the Fourth Circuit was March 6, 1981 and is unpublished.

(iii) The statutory provision believed to confer on this Court's jurisdiction to review the judgment below by writ of certiorari is 28 U.S.C. 1254(1).

(f) The Constitutional provision and statutes which this case involves are:

Title 26, U.S.C. Section 165 § (a), (b), and (c) (1) (2).

Title 26, U.S.C. Section 166 § (a) (1) (d) (1), (2) (A) (B).

STATEMENT OF THE CASE

Jenice Brown Hamrick owned a one half interest in a 936 acre farm. She had no funds with which to buy seeds, fertilizer, machinery or to pay labor (Appendix page 41-43). Nor was she capable of managing the farm herself (Appendix page 41-43).

In order to run the farming business and make a profit she agreed to execute a mortgage to secure a note of a family corporation, in exchange for that corporations agreement to advance all the necessary funds, furnish the labor and management, and operate the farm for her. The corporation had machinery, management, grain storage, and a cotton gin, and all things necessary to keep the farm in operation, and was run by her brother who owned the other one half interest in the 936 acre farm. (Appendix page 41-43).

Several bad farming years made it impossible to pay the mortgage and the mortgage was foreclosed and she lost her one half

interest in the farm, which she had pledged in order to try to operate the farm at a profit. (Appendix page 9).

She filed a joint return with her husband and deducted the loss. The Commissioner denied the deduction and the matter went to the Tax Court, which decided that the loss was a "non-business bad debt", and only dedeductible as a short term capital loss. The United States Court of Appeals for the 4th Circuit affirmed.

ARGUMENT

Even if the taxpayers action in pledging the property for the corporation in exchange for the corporation's services and farming the land, resulted in some additional benefits to the corporation, such as greater utility of machinery and labor and the ginning of petitioners' cotton, this would not deprive her of the deduction because the primary motive for the mortgaging of her property was to secure funds to operate the farm at a profit.

She had no business other than the farm (Appendix page 42, 43). She had to run this farm the best way she could without any funds of her own. The only way she could run this farm was to get the corporation to do it for her, and the only way she could get the corporation to do it for her was to permit the place to be mortgaged in order for the corporation to obtain sufficient funds to farm it (Appendix page 42, 43). If she had been able to hire an overseer, borrow money to buy farm

machinery, seed, fertilizer, and then lost the place, it certainly would have been deductible.

Surely the fact that her financial condition was such that she could not operate the place herself through an overseer (she had only a one half interest) does not prevent her from deducting the real losses, which occurred because everyones effort to make a profit from the farm failed and the mortgage was foreclosed.

It now appears to petitioner that the loss was deductible under several sections of the Internal Revenue code.

TITLE 26, UNITED STATES CODE ANNOTATED SECTION 165 subsections (a), (b), (c), reads as follows:

"(a) General rule -- There shall be allowed as a deduction any loss sustained during the taxable year and not compensated for by insurance or otherwise.

(b) Amount of deduction -- For purposes of subsection (a), the basis for determining

the amount of the deduction for any loss shall be the adjusted basis provided in section 1011 for determining the loss from the sale or other disposition of property.

(c) Limitation on losses of individuals -- In the case of an individual, the deduction under subsection (a) shall be limited to --

(1) losses incurred in a trade or business;

(2) losses incurred in any transaction entered into for profit, though not connected with a trade or business;

Surely this loss was deductible under 165 (c) (1) and (2).

All the cases under this section hold that if the taxpayer engages in the transaction either in connection with a trade or business or with the intent to make a profit, the losses are deductible.

This proposition is supported by the following cases:

In the case of Jefferson Patterson and Marvin Patterson v. United States, 459 F.2d

487 is found the following language on page 494:

> "It might be concluded by exercise of hindsight that plaintiff did not operate Point Farm in the most efficient manner possible. However, it is not the quality of plaintiff's judgment in attempting to make Point Farm profitable that is controlling, but the fact that he made a good faith effort. Mercer v Commissioner of Internal Revenue, supra, 376 F.2d at 711; Lamont v. Commissioner of Internal Revenue, supra, 339 F.2d at 380; Doggett v. Burnet, supra, 65 F.2d at 194; Charles B. Pennington, supra, at 522."

Another which is extremely similar to this case is Mercer v. Commissioner of Internal Revenue, 376 F.2d 708(1967). In this case Petitioner Loy D. Mercer and his older brother Berle Mercer were raised on a cattle ranch in Nebraska. Berle moved to Alaska with his family and a herd of cattle. He acquired a

ranch in the interior of Alaska and began attempting to ranch for profit. His brother Loy moved to Alaska a year or so later, where he continued his college education, and before moving he owned some Angus cattle and traded them for six Angus-Highland cattle, which would survive better in the Alaska climate.

Loy tried twice to get a homestead and couldn't do it. He had no place to keep his cattle. He paid Berle $5,500 one year and $3,500 another year for taking care of his cattle. He sought to deduct this and the Commissioner disallowed it.

In the instant case, petitioner, Jenice Hamrick had a half interest in a farm. She had no way to farm it, she tried to get some way to farm it. The only way she could farm it was to get a corporation, that she and her brother both owned stock in, to use their machinery and farm the place, and in order to do this she had to pledge the place to get the necessary money to farm it.

She was in essentially the same position

as Loy D. Mercer, because she could not do anything with her farm except get the corporation to farm it, and he couldn't do anything with his cattle, except get his brother to keep them. She pledged all the property she had to get her place farmed, and he paid all the money he had to get his brother to look after his cattle.

The discussion of the matter by the Court, on page 710 and 711, is directly in point in this case:

> "It seems clear from a reading of the opinion of the Tax Court that its decision was in essence a conclusion that the taxpayer's venture was not aimed at profit because a reasonable man would not expect a profit from such a venture, and that while he might in future get into such a business, he had not yet done so in the years in question. We are aware that other circuits have insisted that the taxpayer's expectation of profit be both reasonable and in

good faith. See, e.g., Godfrey v. Commissioner of Internal Revenue, 335 F. 2d 82, 84 (6th Cir. 1964), Whitman v. United States, 245 F. Supp. 845 (W.D. La. 1965). Unquestionably, however, in this circuit the rule is that a taxpayer's venture is a trade or business if he has a good faith expectation of profit from that venture, irrespective of whether or not others might view that expectation as reasonable. Hirsch v. Commissioner of Internal Revenue, supra, 315 F.2d at 736, Brooks v. Commissioner of Internal Revenue, supra. We are not alone in this view. See, e.g., Lamont v. Commissioner of Internal Revenue, supra, 339 F.2d at 380, DuPont v. United States, 234 F. Supp. 681 (D.Del.1964). Here the taxpayer entered into a venture with a good faith expectation of profit. Whether that expectation was foolhardy or shrewd is of no moment. The taxpayer expended his effort and capital to the

limit of his available time and resources. There can be no conclusion other than that the taxpayer's venture, though small in results, was a trade or business within the meaning of sections 162 and 165." (Emphasis added)

In petitioners' case there was absolutely no reason except a desire to operate a business and make a profit, no sporting considerations were involved and petitioners took the only course available to them to farm their land. This is shown by the testimony of petitioner, J. Nat Hamrick, which appears on page 41-43 of the Appendix and reads as follows:

"Q During the three years in issue, 1970, 1971 and 1972, did either you or Mrs. Hamrick receive any rental income from Simon Brown's Sons, Incorporated, for the use of the Crum place?

A No, sir. The only thing that we received were pecans and food and things like that. There was not enough money

realized anywhere to pay us any income. The whole thing was in jeopardy at that time.

MR. BATES: No further questions, Your Honor.

THE COURT: All right. You may step down as a witness, Mr. Hamrick. Thank you.

THE WITNESS: Thank you, sir. I might say one other thing, if I can.

THE COURT: All right.

THE WITNESS: I had no alternative -- when my wife's mother gave her the Crum place, I was not able to farm it. I was practicing law and I had no surplus funds to farm it; I couldn't farm it. I had no way to farm it. She only had a half interest. So I -- there was nothing we could do except let Simon Brown's Sons farm it and if there was any surplus money, she could get it; and there was nothing that we could do except pledge the property for Simon Brown's Sons, cause it was a valuable

> piece of property and without it Simon Brown's Sons couldn't run. I had no way to farm it. I couldn't buy the seed, I couldn't buy the fertilizer, I couldn't do anything with it. So to get any income out of it at all, or get the hope of future income, all I could do was say to my brother-in-law that's running Simon Brown's Sons, "All right, we'll pledge the place for you. You run it and maybe we'll get some income out of it in the future." That's all I could do. . . . You're borrowing from hand to mouth and Peter to pay Paul to get seeds and fertilizer and stuff. That's the reason it was done that way."

Another case which strongly supports petitioners position is Fox v. Commissioner of Internal Revenue, 190 F.2d 101 (1951).

This loss was also deductible under Title 26, United States Code Annotated Section 165 (c) (1), as a loss incurred in a trade or business.

The position of the Commissioner of Internal Revenue that this was a "nonbusiness bad debt", is not in accord with the facts. If a farm is not kept in production, no one can make a profit on it. It grows up, weeds take over, taxes accumulate, and in just a few years it will be totally useless and can be restored only by substantial capital expenditures. In order to keep a farming business profitable, the farm must stay in production. Surely her efforts to keep this farm in operation, so a profit could be made on it was a business endeavor, and her losses were occasioned by the bad crop years which caused her business to fail.

Petitioners' Appellants do not understand how the Commissioner could have characterized this loss as a "nonbusiness bad debt". The corporation did not owe petitioners anything. The debt was owed by the corporation to the lending agency and the petitioners pledged their property to guarantee the payment of the corporation debt so

it could obtain funds to farm the property. When the farm could not make the money to pay the debt, foreclosure was instituted and the farm sold.

Under Title 26, United States Code Annotated Section 166 (a) (1) Wholly worthless debts we find the following:

"(a) General rule --

(1) Wholly worthless debts -- There shall be allowed as a deduction any debt which becomes worthless within the taxable year."

Under Section 166 (d)(2) Nonbusiness debt defined, we find the following:

"(2) Nonbusiness debt defined -- For purposes of paragraph (1), the term "nonbusiness debt" means a debt other than --

(A) a debt created or acquired (as the case may be) in connection with a trade or business of the taxpayer; or

(B) a debt the loss from the worthlessness of which is incurred in

the taxpayer's trade or business."

Surely under these paragraphs, petitioners loss was a business bad debt when they had no reason to incur the debt, except to operate the farm - taxpayer's only business - and no way to operate the farm, except to incur the debt. (Appendix page 41-43).

This action is supported by the following cases:

Trent v. Commissioner of Internal Revenue, 291 F.2d 669 (1961), is directly in point where Headnote 2 reads as follows:

> "Employee, who made loans to corporate employer in order to hold his job, could deduct for a business bad debt when loans became worthless. 26 U.S. C.A. (I.R.C.1954) § 166 (d) (2) (A)."

And Justice Friendly states on page 676:

> "Where, as here, it is plain that the loans were made in connection with the taxpayer's "trade or business or rendering services for pay," Folker v.

Johnson, supra, 230 F.2d at page 909, the statutory requirement has been met.

Judgment reversed."

In the case of Schlumberger Technology Corp. v. U.S.A., 443 F.2d 1115, Judge Thornberry, Judge Wisdom and Judge Dier held that the loans in question were proximately related and had a dominate business motivation even though they only related to a secondary part of the taxpayer's business. It is said on page 1122:

"Although the Taxpayer's primary business was measuring physical phenomeonon in the earth for aid in detecting minerals, it also engaged in developing telementary devices and related measurement components for use by military and space agencies. . . . When it became clear that the personnel were not providing the research and knowledge needed by the taxpayer, taxpayer sold ASI. In these circumstances, it is evident that

the ASI transactions were intrigal and necessary acts in the conduct of SWSC's business and were made with a business and not an investment motive. It follows that the ASI stock and debts were not capital assets and that taxpayer's losses were not covered by Section 1232. For the reasons as stated above, the judgment of the District Court is affirmed as dealing with that portion of the judgment dealing with taxpayer's loss on the CSI notes."

To the same effect is Vincent C. Giblin, v. Commissioner of Internal Revenue, 227 F.2d 692. The relevant holding in this case is set forth in Headnote 2, which reads as follows:

"Where a taxpayer, on 11 or 12 occasions between 1926 and 1945, had contributed time, talent, energy and money to exportation of ideas to make money a part from his law practice, lending such aid to these enterprises as he considered

would best accomplish that purpose, he was engaged in the business of dealing in enterprises, and a loss suffered from worthlessness of a loan made to one of these enterprises was deductible in full as a bad business debt."

To the same effect is Mears v. Commissioner of Internal Revenue, 272 F.2d 788. It cites with approval U.S. Tax Court in Dorminey v. Commissioner, 26 Tax Court 940 (August 1956). Here the petitioner made a loan to United States and Panama Navigation Company in which he was an officer and stockholder. The loan was made to insure a steady supply of bananas. Petitioner's economic motive in making the loans was to further his principal business of food distribution. The Tax Court held that the loans, which later became worthless, "were so incidental and proximately related to his true business that the taxpayer was allowed to deduct the amount of the loans as business bad debts." . . . "The Tax Court said, "Whether or not the

petitioner, by his financing activities, was engaged in the money lending business may not be determined since the bad debt loss was incidental to and proximately related to his produce business.'"

We now come to the question of the value of the Crum Place Farm in the year 1920, when it was given to Zelma Brown. At the hearing in Winston-Salem, North Carolina, the Government's witness, Mr. Cox testified that he had investigated the matter and gave his opinion as to the value of the land at that time by looking at comparables as shown by the records which allegedly represented what land was sold for during that period. In his testimony he recited the fact that he did not contact anyone who was living at the time and who had personal knowledge of the matter (Appendix page 32, 33). He testified that he considered only the value of the land itself with no improvements (Appendix page 32). Mr. Cox testified that if it appeared that the property contained a cotton gin, a seed storage

warehouse, 10 dwelling, cotton seed storage warehouse and a grain storage warehouse, it would change the value of the property and he would be valuing a business and not bare farmland (Appendix page 34). He said that if he had been called on to evaluate the property in 1920, he would have taken into consideration the value of all the improvements, (Appendix page 34) and further testifying that this was a very good cotton plantation. (Appendix page 33).

In his testimony, Stanley Brown stated that in 1920 he was a student at the University of Virginia (Appendix page 35, 36) and was 16 years old and worked for his father. That he assisted in the supervision of the Crum Place Farm and that he was familiar with the improvements on the property (Appendix page 35, 36). That at that time, there was a large overseer's house, containing six or seven bedrooms, bathroom facilities; that there was a windmill, a large barn and yard where mules and livestock were kept, a cow

barn, a syrup mill and a cotton gin; that there was a deep well for water and a telephone line that they had constructed themselves for a distance of six miles. (Appendix page 35, 36). That it had an asparagus packing house and a large pecan orchard. (Appendix page 37). That it had storage facilities for cotton seed and all other farm products on the place. (Appendix page 38) That this plantation was unique in that in that area of South Carolina many times a farm would have large amounts of bad land and large amounts of good land. That the Crum Place Farm had very little of what was called bone, land that was unproductive and tha there was not more than 12 acres of bone, unproductive land. (Appendix page 39, 40). That it had between 75 and 90 acres of asparagus, which meant that the crowns were down in the land and were harvested every year. That the property had its own asparagus packing house. That some of this land was black cucumber bottom land, consisting of

about 100 acres, which was very productive and that also located on the property was a cucumber packing shed. (Appendix page 38).

In the deposition of Winchester Graham, who was deposed on September 29, 1977, in Columbia, South Carolina, he stated that he was living in Denmark, South Carolina, about six miles from the Crum Place Farm in 1920. (Appendix page 29). That he was familiar with the property and that it had a cotton gin and grain storage and dwellings on it. (Appendix page 29). That this property and the Guess property was the best property in that part of the State. (Appendix page 29). He stated on page 5 of the record that he valued this property against ordinary open land in that part of South Carolina to be four times what the ordinary land would be valued at, and specifically stated as follows:

> "Q Now, suppose that this other land that was sold there is open land with good fertile land, how much more would

you say that this working plantation with everything on it would be worth?

A Well, I'd rather take it on a percentage. I'd say, if you have a dollar over here, you'd get about four dollars over here (Indicating) per acre. I'd say about four to one, but I'm taking the poorest part of Barnwell County against the better part of Barnwell County.

Q Now, if Mr. Bates has sales somewhere in this area for open land that was bringing sixty to eighty dollars an acre and my father-in-law had a complete working plantation with cotton gin and everything on it, how much more would you say that it would be worth than the other?

A I'd say at least three or four times." (Appendix page 28).

Further on page 6 upon cross examination, Mr. Graham testified that he was 24 years old in 1920 and that he did not know of any land

in the area as good as the Crum Place Farm, except the Guess property located about four or five miles away. (Appendix page 29).

Mr. Walter Frederick Marvin was deposed on September 29, 1977, as to value and stated that he was 85 years old; that he remembered in the '20's that the Crum Place Farm had tenant houses and a cotton gin. (Appendix page 30). He testified on page 2 of the record that from his opinion of land being traded in the area, he felt that the Crum Place Farm was worth at least $250.00 an acre because the land was extremely fertile and in good shape and that the Crum Place Farm and the Guess property were the two most valuable places in the area. (Appendix page 30).

CONCLUSION

In conclusion, petitioners respectfully submit that the mortgaging of the land for Simon Brown's Sons was dominately motivated by business considerations - was entered into

for profit - and it was the only thing petitioners could do to operate the Crum Place Farm and was deductible from income under the code sections referred to herein.

Petitioners also contend that the operation of the Crum Place Farm was the only business of Jenice B. Hamrick and that she could not operate it except through Simon Brown's Sons and Simon Brown's Sons could not finance the operation without the funds raised by mortgaging the Crum Place Farm and, therefore, the mortgage and loss of the property was for business reasons and a business bad debt loss.

That the fair market value of the Crum Place farm as of December 20, 1920, which is the basis year, was at least $250.00 an acre and that Taxpayers' loss was at least $125,000.00.

Respectfully submitted, this the _____ day of June, 1981.

J. Nat Hamrick

Jenice B. Hamrick

PETITIONERS

Hamrick & Hamrick
P. O. Drawer 470
Rutherfordton, NC 28139
Counsel for Petitioners

CERTIFICATE OF SERVICE

This is to certify that the undersigned, a member of the bar of this Court, served this Petition for a Writ of Certiorari and Appendix thereto upon all the parties to this action by depositing at least three copies of the Petition and three copies of the Appendix in the United States mail addressed to the attorneys whose names and post office address are:

M. Carr Ferguson, Asst. Attorney General
Gilbert E. Andrews
Jonathan S. Cohen
Jay W. Miller, Attorneys
Tax Division, Department of Justice
Washington, D.C. 20530

This 2 day of June, 1981.

J. Nat Hamrick
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Appendix To

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UNPUBLISHED

UNITED STATES COURT OF APPEALS

FOR THE FOURTH CIRCUIT

No. 79-1578

J. Nat and Jenice B. Hamrick,

Appellants,

v.

Commissioner of Internal Revenue,

Appellee.

Appeal from the United States Tax Court, Charles R. Simpson, Tax Court Judge.

Submitted: December 12, 1980

Decided: March 6, 1981

Before PHILLIPS, MURNAGHAN and SPROUSE, Circuit Judges.

(J. Nat and Jenice B. Hamrick, Appellants Pro Se. Gilbert E. Andrews. Chief, Appellate Section; M. Carr Ferguson, Assistant Attorney General, Tax Division-Department of Justice; Jonathan S. Cohen; Jay W. Miller, Tax Division-Department of Justice; on brief for the Appellee.)

PER CURIAM:

J. Nat and Jenice Hamrick appeal the tax court's decision in a case involving their federal income tax liability for the years 1970, 1971, and 1972. The tax court decided that a loss claimed by them to be a business bad debt was in fact a nonbusiness bad debt deductible as short term capital loss. See 26 U.S.C. § 166 (d). The court also held that taxpayers' basis in the property in issue was $39,780 rather than $170,000, as claimed by the Hamricks. The court therefore ruled that deficiencies were due from the Hamricks for the years in question.

The Tax court thoroughly analyzed the issues presented in the case. Nothing the Hamricks assert in this appeal alters the validity of that court's judgment. We dispense with oral argument as the facts and legal arguments are adequately presented in the briefs and record and the decisional process would not be significantly aided by oral argument. We affirm the decision below

on the reasoning of the tax court. Hamrick v. Commissioner, T.C. Memo. 1979-72 (March 5, 1979, June 13, 1979).

AFFIRMED.

T.C. Memo. 1979-72

UNITED STATES TAX COURT

J. NAT and JENICE HAMRICK, Petitioners v. COMMISSIONER OF INTERNAL REVENUE, Respondent

Docket No. 7250-75. Filed March 5, 1979.

(1) P, a 41-percent shareholder in a family corporation, sustained a loss upon the foreclosure and sale of a one-half interest in property that was being farmed by such corporation and that she had mortgaged to secure loans for the corporation. Held, such loss resulted from a nonbusiness debt becoming worthless during the year.

(2) Since P acquired the property by gift, both parties agreed that P's basis in the property equaled its fair market value on Dec. 7, 1920. Held, such value determined.

J. Nat Hamrick, pro se.

Mathew E. Bates, for the respondent.

MEMORANDUM FINDINGS OF FACT AND OPINION

SIMPSON, Judge: The Commissioner determined the following deficiencies in income

taxes and additions to tax of the petitioners:

Year	Deficiencies	Additions Sec. 6651(a)(1) I.R.C. 1954[1]	Additions Sec. 6653(a) I.R.C. 1954
1970	$11,215.91	$1,121.59	$587.71
1971	14,595.49	1,459.55	759.02
1972	6,694.16	1,673.54	703.36

The petitioners concede their liability for the additions to tax under sections 6651(a)(1) and 6653(a) with respect to any deficiency determined by the Court; the only issues remaining for decision are: (1) Whether the loss the petitioner sustained upon the foreclosure and sale of a one-half interest in property that she had mortgaged to secure loans to a corporation which farmed such property is deductible as a business bad debt under section 166; and (2) what was the fair market value of the property on December 7, 1920.

---

[1] All statutory references are to the Internal Revenue Code of 1954 as in effect during the years in issue.

FINDINGS OF FACT

Some of the facts have been stipulated, and those facts are so found.

The petitioners, J. Nat and Jenice Hamrick, are husband and wife who maintained their legal residence in Rutherfordton, N.C., when they filed the petition herein. They filed their joint Federal income tax returns for the years 1970 and 1971 with the Southeast Service Center, Chamblee, Ga.; their joint Federal income tax return for 1972 was filed with the Memphis Service Center, Memphis, Tenn. Mrs. Hamrick will sometimes be referred to as the petitioner.

On December 7, 1920, the petitioner's father conveyed a 936-acre tract of land in Bambery County, S.C., to the petitioner's mother by deed of gift. The land, known as the Crum Place (the property), consisted of high quality farming land suitable for the growing of cotton, pecans, asparagus, cucumbers, and other crops. The property also included some 20 houses for the farm's workers,

an overseer's home with six or seven bedrooms, a large barn, windmill, syrup mill, Lummus cotton gin, storage faciilities and packing houses for the crops, a well for water, and a privately constructed and maintained telephone line. The farm also maintained some mules and livestock.

On August 1, 1961, the petitioner's mother mortgaged the property, along with six other tracts of land, to secure a debt of Simon Brown's Sons, Inc. (the corporation). On October 30, 1963, the petitioner's mother conveyed a one-half interest in the property to the petitioner by deed of gift, reserving a life estate in herself. On September 28, 1964, the petitioner reconveyed her one-half interest in the property to her mother by deed of gift. On November 4, 1964, the petitioner's mother executed a new mortgage on the property to replace the mortgage of 1961. On November 27, 1964, the petitioner's mother reconveyed the one-half interest to the petitioner subject to a life estate. In

1966, the petitioner again reconveyed her one-half interest in the property to her mother, and her mother executed a new mortgage to replace the earlier mortgages on the property; thereafter, she reconveyed the one-half interest to the petitioner. Later in 1966, the petitioner joined in the execution of a junior mortgage on the property to secure a loan to the corporation. In 1967, the petitioner joined in the execution of a new junior mortgage to replace the 1966 junior mortgage on the property and to secure additional loans to the corporation. From July 23, 1966 until October 1, 1970, the petitioner and her brother owned the property jointly as tenants in common subject to a life estate in their mother.

From 1963 to 1972, the petitioner was a shareholder in the corporation, which was a family corporation. The capital stock of the corporation was owned as follows:

Stockholder	Percent of Stock Owned
Jenice Brown Hamrick	41
D. Stanley Brown	41
Zelma Brown	18

Zelma Brown is the petitioner's mother; D. Stanley Brown is the petitioner's brother, who ran the corporation and earned his living by such work. Under an informal arrangement, the owners of the property allowed the corporation to farm the property. The corporation owned all the necessary farming equipment, provided all the seed, fertilizer, labor, and supervision for the farm, and marketed all the crops from the property. During the years in issue, the petitioner received no rent from the corporation for the use of the property. However, she did receive pecans and other food from the corporation.

On October 1, 1970, the junior mortgage on the property was foreclosed upon, and the mortgagee purchased the property at the foreclosure sale for $200,000.

In their tax return for 1970, the petitioners deducted an ordinary loss of $170,000

attributable to the petitioner's loss of her one-half interest in the property and carried forward a net operating loss of $38,898 to 1971. Schedule D of such return included the statement: "Land placed as collateral on loan for brother's business. Loan not repaid and business bankrupt. Land was seized by referee to cover part of loss. Is ordinary loss under bad debt heading." In his notice of deficiency, the Commissioner reduced the petitioner's adjusted basis in the property to $32,180. He also determined that the petitioners realized a long-term capital loss of $32,180, subject to the limitation of section 1211, and that there was no net operating loss to carry forward to 1971.

OPINION

The first issue to be decided is whether the petitioner sustained an ordinary loss as a result of the foreclosure on her interest in the property. There is some confusion as

to the petitioners' position in this case.[2] On their return, they referred to the loss as a bad debt; but in their petition and in their brief in this case, they referred to it as a loss incurred in the carrying on of a trade or business within the meaning of section 165 (c)(1), although they rely on cases dealing with claims for bad debt deductions. The Commissioner, at trial and in his brief, now maintains that the loss must be treated as a nonbusiness bad debt.

Section 165(a) allows a deduction for any loss sustained during the taxable year that is not compensated for by insurance or otherwise, but section 165(c) limits the deductions allowable to individuals. Section

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[2] It is clear that the petitioners are not claiming that the loss was deductible under sec. 165(c)(2) as a loss incurred in a transaction entered into for profit, or that the loss was deductible under sec. 212 as an expense incurred for the production or collection of income, or for the management, conservation, or maintenance of property held for the production of income.

165 (c)(1) allows an individual a deduction for a loss incurred in a trade or business. However, the deduction for bad debts is set forth in section 166(a), which allows a deduction for a debt which becomes worthless during the taxable year.

The loss in this case was not sustained upon the foreclosure and sale of the property. The Supreme Court held in Putnam v. Commissioner, 352 U.S. 82 (1956), that a loss sustained by a guarantor unable to recover from the debtor is a loss from a bad debt to which the guarantor becomes subrogated upon discharging his liability as guarantor. By mortgaging her property to secure the loans, the petitioner was in effect placing her property as collateral for the loans and acting as a guarantor of the loans. The petitioner then became subrogated to the debt between the corporation and its creditors upon the foreclosure and sale of the property, and the loss she sustained when she was unable to recover from the corporation was a bad

debt loss deductible under section 166.

Moreover, in Spring City Foundry Co. v. Commissioner, 292 U.S. 182 (1934), the Supreme Court held that the predecessors of sections 165 and 166 are mutually exclusive; that is, a bad debt, although a loss, cannot be deducted under the general loss provisions of section 165. Therefore, we must hold that the loss the petitioner sustained upon the foreclosure and sale of her interest in the property is not deductible as a business loss under section 165(c)(1).

Section 166(d) provides:

"(d) Nonbusiness Debts.--

(1) General rule.--In the case of a taxpayer other than a corporation--

(A) Subsections (a) and (c) shall not apply to any nonbusiness debt; and

(B) Where any nonbusiness debt becomes worthless within the taxable year, the loss resulting therefrom shall be considered a loss from the sale or exchange, during the taxable year, of a capital asset held for not more than 6 months.

(2) Nonbusiness debt defined.--For purposes of paragraph (1), the term "nonbusiness debt" means a debt other than--

(A) a debt created or acquired (as the case may be) in connection with a trade or business of the taxpayer; or

(B) a debt the loss from the worthlessness of which is incurred in the taxpayer's trade or business."

Thus, we must decide whether the petitioner's claim against the corporation was a business or a nonbusiness debt within the meaning of section 166(d).

Section 1.166-5(b), Income Tax Regs., defines nonbusiness debts:

"(b) Nonbusiness debt defined. For purposes of section 166 and this section, a nonbusiness debt is any debt other than--

(1) A debt which is created, or acquired, in the course of a trade or business of the taxpayer, determined without regard to the relationship of the debt to a trade or business of the taxpayer at the time when the debt becomes worthless; or

(2) A debt the loss from the worthlessness of which is incurred in the taxpayer's trade or business.

> The question whether a debt is a non-business debt is a question of fact in each particular case. The determination of whether the loss on a debt's becoming worthless has been incurred in a trade or business of the taxpayer shall, for this purpose, be made in substantially the same manner for determining whether a loss has been incurred in a trade or business for purposes of section 165(c)(1). For purposes of subparagraph (2) of this paragraph, the character of the debt is to be determined by the relation which the loss resulting from the debt's becoming worthless bears to the trade or business of the taxpayer. If that relation is a proximate one in the conduct of the trade or business in which the taxpayer is engaged at the time the debt becomes worthless, the debt comes within the exception provided by that subparagraph. * * *[Emphasis added]"

In United States v. Generes, 405 U.S. 93 (1972), the Supreme Court held that in determining whether a bad debt has a "proximate" relation to the taxpayer's trade or business within the meaning of the regulations, we must consider the taxpayer's "dominant motivation" for extending the loan. 405 U.S. at 103. In that case, a 44-percent shareholder in a family corporation deducted loans he made to the corporation as a business bad debt, claiming that such loans were made for business reasons, that is, to preserve his salary as

president of the corporation. The Supreme Court said:

> "We conclude on these facts that the taxpayer's explanation falls of its own weight, and that reasonable minds could not ascribe, on this record, a dominant motivation directed to the preservation of the taxpayer's salary as president of Kelly-Generes Construction Co., Inc. [405 U.S. at 107.]"

The petitioner contends that she sustained an ordinary business loss upon the foreclosure and sale of her interest in the property. She asserts that the operation of the property was her "only business", but also states that she could not operate the property without the corporations. Yet, the corporation could not finance the business without the funds provided by the mortgaging of the property. Therefore, the petitioner concludes that the mortgaging of the property and the resultant foreclosure and loss were for business reasons. However, after consideration of all the evidence, we cannot conclude that the petitioner's dominant motivation for mortgaging the property, and subsequent subrogation to the claims against the

corporation, was for business reasons.

The phrase "trade or business", as used in the Federal tax laws, has a "common and well-understood connotation as referring to the activity or activities in which a person engages for the purposes of earning a livelihood." Folker v. Johnson, 230 F.2d 906, 907 (2d Cir. 1956). The petitioner has the burden of proving that her claim against the corporation qualified as a business debt. Rule 142, Tax Court Rules of Practice and Procedure; Welch v. Helvering, 290 U.S. 111 (1933); see Scifo v. Commissioner, 68 T.C. 714, 723 (1977). She does not allege that she was engaged in the business of farming the property, or that she was a farmer in general. The business of farming the property was conducted by the corporation and was not her individual business. Moreover, even though the petitioner was a 41-percent shareholder of the stock of the corporation that farmed the land, the business of the corporation is not attributable to her. It is a well settled principle that a share-

holder has a separate identity from the corporation and that the business of a corporation is not the business of its shareholders or offiers. Burnet v. Clark, 287 U.S. 410 (1932); Dalton v. Bowers, 287 U.S. 404 (1932); Omaha Nat. Bank v. Commissioner, 183 F.2d 899 (8th Cir. 1950), affg. a Memorandum Opinion of this Court. Mere participation in a corporation by owning stock does not place one in the business of the corporation. Even devoting one's time and energies to the affairs of a corporation is not of itself, without more, the trade or business of the person so engaged. Whipple v. Commissioner, 373 U.S. -93, 202 (1963). If the funds secured by the mortgages enabled the corporation to prosper, the petitioner might share in the profits as a shareholder of the corporation, but in that event, the loans merely enhance her dividends. Therefore, we hold that the petitioner has failed to show that the claim was a business debt because of her interest in the corporation.

Nor has the petitioner shown that the debt was proximately related to her interest as an alleged lessor of the property to the corporation. This Court has stated that ordinarily the rental of property constitutes a trade or business. Lagreide v. Commissioner, 23 T.C. 508 (1954); Hazard v. Commissioner, 7 T.C. 372 (1946). We recognize that it is not always necessary to show the actual receipt of rental income to establish that one is engaged in the trade or business of renting property. See, e.g., Crawford v. Commissioner, 16 T.C. 678 (1951). However, the nominal renting of property does not convert it into business use, and the courts have generally looked to the taxpayer's expectation of receiving a profit from the rental of property. See Johnson v. Commissioner, 19 T.C. 93 (1952); Crawford v. Commissioner, supra. Here, the petitioners admitted that they received no rental income from the property during the years in ussue, and they failed to prove that they ever received any

rental income from the property. Accordingly, we must conclude from the evidence presented that the "renting" here was nothing more than nominal and that the petitioner had no expectation of receiving a profit.

In addition, the petitioner has offered no evidence that there was any real leasing arrangement with the corporation. She has not introduced the terms of any lease with the corporation, the duration, if any, of a lease, nor evidence as to the amount the corporation would pay her under the arrangement. Mr. Hamrick testified that "if there was any surplus money, she could get it." Such an informal arrangement does not place the petitioner in the trade or business of renting the property to the corporation.

Indeed, an examination of all the facts and circumstances suggests that the petitioner allowed the corporation to farm her one-half of the property as an accommodation to her brother in order to preserve his job with the corporation. Mr. Hamrick testified that "We

had no alternative to this, because Stanley Brown had no way to live except running Simon Brown's Sons * * *." On this reocrd, we hold that since the petitioner was not engaged in either the trade or business of farming or renting the property, the loss she sustained upon the uncollectibility of the loans to which she was subrogated was a nonbusiness bad debt.[3]

The second issue for consideration is the fair market value of the property on December 7, 1920. Since the petitioner received the property as a gift from her mother, her basis in the property is determined under section 1015. Section 1015 (a) provides:

> "(a) Gifts after December 31, 1920.--If the property was acquired by gift after December 31, 1920, the basis shall be the same as it would be in the hands

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[3] The Commissioner did not argue that the foreclosure and sale of the property was a taxable transaction. See Helvering v. Hamel, 311 U.S. 504 (1941). Therefore, we give no consideration to that issue.

> of the donor or the last preceding owner by whom it was not acquired by gift, except that if such basis (adjusted for the period before the date of the gift as provided in section 1016) is greater than the fair market value of the property at the time of the gift, then for the purpose of determining loss the basis shall be such fair market value. If the facts necessary to determine the basis in the hands of the donor or the last preceding owner are unknown to the donee, the Secretary shall, if possible, obtain such facts from such donor or last preceding owner, or any other person cognizant thereof. If the Secretary finds it impossible to obtain such facts, the basis in the hands of such donor or last preceding owner shall be the fair market value of such property as found by the Secretary as of the date or approximate date at which, according to the best information that the Secretary is able to obtain, such property was acquired by such donor or last preceding owner."

The parties have agreed that the petitioner's basis in the property should be determined by the property's fair market value on December 7, 1920.

The Commissioner determined that the value of the property on December 7, 1920, was $85 per acre. He based this determination on the report of a valuation expert. In preparing his report, such expert spent 3 days in the

area in which the property is located. He inspected the subject property, looked at other property in the general area, and talked with soil conservation specialists about soil studies they had just completed on the land. He then examined records of sales of farm land in the area from 1919 to 1922. The expert used about 13 comparable sales to determine that the fair market value of the property in this case in 1920 was $85 per acre. One sale he considered was a tract of land on the left border of the property that was sold on February 7, 1920, for $85 per acre. The expert recognized that the land on that property was very good and equal to the land on the subject property for the production of cotton. In some of the comparable sales, the land was sold for as little as $50 per acre. In reaching his conclusion, the expert did not include any amount for the improvements on the property.

The petitioner asserts that the fair market value of the land on December 7, 1920,

was at least $250 per acre, and she contests the Commissioner's value on the ground that his expert failed to consider all the relevant facts in arriving at his estimate. Particularly, she contends that the Commissioner's expert failed to take into consideration the quality of the land on the subject property, the size of such property, and the extensive improvements thereon. To support her position, the petitioner called two witnesses, one of whom expressed the view that the property was worth $250 per acre in 1920. Such witnesses also testified as to the quality of the property and the improvements thereon. However, neither witness had any expertise in valuing land, nor did either support his opinion by reference to comparable sales in the area.

In this case, we are impressed by the opinion of the Commissioner's expert. He was qualified to express an opinion on the value of land, and his opinion was based on a thorough and careful analysis of comparable

sales in the area--a generally accepted method of valuing land. Crane v. Commissioner, 49 T.C. 85, 94-95 (1967); Huron Building Co. v. Commissioner, 15 B.T.A. 1107, 1114 (1929), affd. sub nom. Tracy v. Commissioner, 53 F.2d 575 (6th Cir. 1931), cert. denied 287 U.S. 632 (1932). His opinion appears to have taken into consideration both the quality of the property and its size. On the other hand, the petitioner's witnesses lacked expertise, and their opinions were not grounded on objective facts.

The most significant difference of opinion involved the treatment of the improvements. Under section 1016, the basis of the property must be adjusted to take into consideration any depreciation allowed or allowable on those improvements. See Pittsburgh Terminal Corp. v. Commissioner, 60 T.C. 80, 87 (1973), affd. in an unpublished opinion 500 F.2d 1400 (3d Cir. 1974); Moorhead & Sons, Inc. v. Commissioner, 40 T.C. 704, 713 (1963). The Commissioner determined

that all such improvements would be fully depreciated by 1970, and the petitioner has presented no evidence to indicate otherwise. Accordingly, the Commissioner's expert was correct in basing his opinion on the value of the land without taking into consideration any improvement thereon, and since it is clear that the petitioner's witnesses included the value of the improvements in their opinions, such fact provides another reason for not accepting their opinions.

In conclusion, we find and hold that the value of the property on December 7, 1920, was $85 per acre. In his notice of deficiency, the Commissioner determined the total value of the petitioner's interest in such property to be $32,180. However, his expert found that the total value of her interest was $39,780, and in his brief, the Commissioner adopted such value. This, in their computations for decision in accordance with Rule 155, Tax Court Rules of Practice and Procedure, the parties should use the figure

of $39,780 as the basis of the petitioner's interest in the property.

Decision will be entered under Rule 155.

Q Now, suppose that his other land that was sold there is open land with good fertile land, how much more would you say that this working plantation with everything on it would be worth?

A Well, I'd rather take it on a percentage. I'd say, if you have a dollar over here, you'd get about four dollars over here (Indicating) per acre. I'd say about four to one, but I'm taking the poorest part of Barnwell County against the better part of Barnwell County.

Q Now, if Mr. Bates has sales somewhere in this area for open land that was bringing sixty to eighty dollars an acre and my father-in-law had a complete working plantation with cotton gin and everything on it, how much more would you say that it would be worth than the other?

A I'd say at least three or four times.

Q How old would you have been in 1920?

A Well, I got married when I was nineteen and that was 1915, so that would have made me about twenty-three or twenty-four years old. We moved to Columbia in '23. We were living there--I was born and raised in Bambery which is the county seat and my father was a lawyer.

MR HAMRICK: That was just a few miles from this property?

A Yes.

Q Do you know if there was any other land in the area where the Crum place was located that, as far as the soil was concerned was as good as the Crum place?

A There might have been some land, but I would say that I would pick that out, that and the Guess property as two of the best pieces of property in the county, . . .

Q Well, from what you know about land being traded in this area, do you have an opinion satisfactory to yourself, as to what that place was worth in December, 1920?

A Well, that's been a good long time and land varied in the price at that time, but that was extra good land and so many buildings and all, I know that it was worth two fifty, at least.

Q Two hundred fifty dollars an acre?

A Yes, and this Guess place out here, that's good land too, that is all worth about that price.

Q Would you say that that was the two best pieces of land around?

A Well, it was extra good land because they were good farmers and they knew what they were doing and they kept the land in good shape. I bought a lot of land myself. I Bought three hundred eighty-five acres a good bit cheaper than that but it was poor

land, a lot of it was poor land and you had to build it up.

Record of Hearing at Winston-Salem, North Carolina on September 12, 1977, Page 10-12

Testimony of James Cox

BY MR. HAMRICK:

Q Mr. Cox, you say that you only considered the value of the land itself with no improvements.

A That is correct.

Q So if it should appear from evidence later that this property contained a cotton gin, a seed storage warehouse, a -- 10 dwellings and a cotton seed storage -- and a grain storage warehouse, that would change your valuation as to the property, would it not, sir?

A It would change the value -- I would be valuing a business and not bare farmland.

Q I see. Now, in your comparables you went to the public records, I believe.

A Yes, sir.

Q And you were not able to verify from people who bought and sold this land actually what was paid for it, were you?

A No, sir, I was not, because --

Q So long ago.

A -- they were not living.

Q Yes, sir.

A It was, you know, 1920, it was very difficult to find people that -- the sellers and buyers, and that's why. I realize normally that it should be done.

Q Yes, sir, I understand. Now, the prices that you got here were gotten off of tax stamps or recitals in deeds, or something of that sort.

A That is correct.

Q Now, I believe you said in your report that this was a very good cotton plantation.

A Yes, sir, it was very good.

Q So a value of the whole property, with all the improvements on it -- the houses and the cotton gin and grain storage and so forth -- if you had been called to evaluate

that in 1920, to value the whole property, you would have certainly taken into consideration the value of the improvements, wouldn't you?

A Yes, sir, I would have if I'd been called to value the business rather than the --

Q Yes.

A -- land only.

Q Yes, sir. I believe this land's located about six or seven miles from Denmark, South Carolina?

A Yes, sir. I have my location map in my report.

Q Yes, sir.

A Good accessibility.

Q Thank you, sir.

Record of Hearing at Winston-Salem, North Carolina on September 14, 1977, pages 13-15

Testimony of D. Stanley Brown

A I assisted in its supervision.

Q Now, Mr. Brown, will you tell us what was on the Crum place other than the land in December of 1920.

A I believe that there were about 20 farm houses where the people that worked for us lived. In addition to that there was an overseer's home that was a very nice home, indeed. It was a large house -- it's still there -- and I would say that that house -- it was one and a half stories high and I would say that it had about six or seven bedrooms. It had bathroom facilities, it had a windmill for -- to supply water, it had a very large barn in the yard where the mules were kept and the livestock, it had a cow barn on the back of the place, it had a syrup mill, it had a gin house that was modern at that time. It had modern facilities.

Record of Hearing at Winston-Salem, North Carolina on September 14, 1977, pages 13-15 continued, Testimony of D. Stanley Brown

Q When you say "gin house," are you referring to cotton gin?

A It was a cotton gin, yes, sir, and it was operated -- it had been converted from a boiler to electrical. It was operated with electrical motor, electric motors. There was a Lummus cotton gin, was the make of the gin. It had -- I'd say it had a good deep well for water. It had something that was rather unique to the farm. We built a telephone line all the way from Southern Bell's mainline in Denmark to the Crum place, a distance of about six miles, and we owned and maintained that line and kept it -- had to keep it -- in other words, we had to put up the poles and had to keep the line in workable order, so that we could use -- in order to keep from having to go out there to contact the foreman and to give orders. It had an

asparagus packing house, because we were growing asparagus on the farm. Of course, it had its horses and mules and buggies and wagons and --

Q That's not relevant to this.

A -- that type of thing, the farming equipment that went with the farm. But on the land itself -- of course, there were certain crops that were planted on the farm that were no -- in other words, like asparagus. You planted asparagus once every 15 years. Well, it had a certain acreage of asparagus where the crowns were there and then it had a pecan orchard, a very large pecan orchard, and those were grafted trees that were Schleys and Stewarts. They were very heavily, heavy producting trees. Then it had a pecan orchard that lined the road all the way through the place on both sides of the

highway. I'm trying to give you --

Q Did you have any seed storage facilities, Mr. Brown?

A Sir?

Q Did you have any cotton seed storage facilities?

A We had storage facilities for all farm products on the place. We had storage facilities for where we kept the containers for the cucumber, when we harvest them, cucumber crates -- or they were -- in those days they were not tubs, they were baskets. We had a cucumber basket container storage. We had feed storage and -- where we stored the crops for the livestock and for sale.

Record of Hearing at Winston-Salem, North Carolina on September 14, 1977, page 16-17

Testimony of D. Stanley Brown

Q Now, Mr. Brown, you have described improvements on the property. Would you describe the land itself and any --

A The land itself?

Q Yes, sir.

A I shall do my best, sir. In our area of the South Carolina the quality of land varies considerably. There will be land that is extremely valuable and next to it will be land that is extremely invaluable. The Crum place was unique in that there was approxiamtely a thousand acres of all good land, which was something that was very, very unusual, to find a large plantation where there was very little of what we called bone, land that was unproductive. And of the entire approximate thousand acres in the Crum place -- I think there was somewheres around 980 acres -- I would estimate that there was not more

Record of Hearing at Winston-Salem, North Carolina on September 14, 1977, page 16-17, continued, Testimony of D. Stanley Brown

than 12 acres of bone. We gave that to the colored people to use for a baseball field to play -- to have their games and recreation in -- because we didn't even attempt to farm it. It was like a little sand -- sandy area. But there was very little wooded land. . . .

Record of Hearing at Winston-Salem, North Carolina on September 14, 1977, pages 29-30

Testimony of J. Nat Hamrick

Q During the three years in issue, 1970, 1971 and 1972, did either you or Mrs. Hamrick receive any rental income from the Simon Brown's Sons, Incorporated, for the use of the Crum place?

A No, sir. The only thing that we received were pecans and food and things like that. There was not enough money realized anywhere to pay us any income. The whole thing was in jeopardy at that time.

MR. BATES: No further questions, Your Honor.

THE COURT: All right. You may step down as a witness, Mr. Hamrick. Thank you.

THE WITNESS: Thank you, sir. I might say one other thing, if I can.

THE COURT: All right.

THE WITNESS: I had no alternative -- when my wife's mother gave her the Crum place, I was not able to farm it. I was practicing

law and I had no surplus funds to farm it; I couldn't farm it. I had no way to farm it. She only had a half interest. So I -- there was nothing we could do except let Simon Brown's Sons farm it and if there was any surplus money, she could get it; and there was nothing that we could do except pledge the property for Simon Brown's Sons, cause it was a valuable piece of property and without it Simon Brown's Sons couldn't run. I had no way to farm it. I couldn't buy the seed, I couldn't buy the fertilizer, I couldn't do anything with it. So to get any income out of it at all, or get the hope of future income, all I could do was say to my brother-in-law that's running Simon Brown's Sons, "all right, we'll pledge the place for you. You run it and maybe we'll get some income out of it in the future." That's

Record of Hearing at Winston-Salem, North Carolina on September 14, 1977, pages 29-30 continued, Testimony of J. Nat Hamrick

all I could do. We had no alternative to this, because Stanley Brown had no way to live except running Simon Brown's Sons and Simon Brown's Sons couldn't run unless this place was pledged cause you couldn't get the money. You're borrowing from hand to mouth and Peter to pay Paul to get seeds and fertilizer and stuff. That's the reason it was done that way.

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No. 80-2053

In the Supreme Court of the United States

OCTOBER TERM, 1980

J. NAT HAMRICK, ET UX., PETITIONERS

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

MEMORANDUM FOR THE RESPONDENT IN OPPOSITION

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MEMORANDUM FOR THE RESPONDENT IN OPPOSITION

The question presented by the petition in this federal income tax case is whether the decision below correctly held that the loss claimed by petitioner [1] arising from the mortgagee's foreclosure on her property which she had encumbered to secure loans to her family-owned corporation was a nonbusiness bad

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[1] References to "petitioner" are to Jenice Hamrick. J. Nat Hamrick, petitioner's husband, is a party only because he filed a joint income tax return with his wife for the years in question.

debt, deductible only as a short-term capital loss, and correctly determined the amount of that loss.

The pertinent facts may be summarized as follows: On December 7, 1920, petitioner's father conveyed by deed of gift a large tract of farm land to petitioner's mother, who mortgaged the property to secure the debts of the family-owned corporation. Subsequently, in 1966, petitioner's mother made a gift of the property, still subject to the pre-existing mortgage, dividing it equally between petitioner and petitioner's brother and reserving to herself a life estate in the property. In 1967, petitioner executed a second mortgage on her one-half interest in the property, as collateral for loans made to her family-owned corporation.[2] Pursuant to an informal arrangement, the corporation, under the direction of taxpayer's brother, farmed this property without paying any rent to petitioner. In 1970, the mortgagee foreclosed on the property, and purchased it at a foreclosure sale for $200,000 (Pet. App. 6-9).

On her income tax return for 1970, petitioner claimed an ordinary loss deduction of $170,000 attributable to the loss on the foreclosure sale of her one-half interest in the property. On audit, the Commissioner of Internal Revenue reduced petitioner's loss on the sale of the property to $32,180, and determined that it was deductible as a long-term capital loss (Pet. App. 9-10). In this proceeding brought by petitioner to redetermine the ensuing deficiencies, the Tax Court characterized the transaction, in which petitioner mortgaged her property for the corporation's debts, not as a sale but as tantamount to a guaranty of those debts, giving rise to subrogation upon the

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[2] Petitioner owned 41% of the corporation's capital stock, while her mother and brother owned the remainder (Pet. App. 9).

ultimate foreclosure by the mortgagee (Pet. App. 12-13). The Tax Court accordingly ruled that the loss suffered by petitioner because of the corporation's inability to repay the obligation arose from the worthlessness of a nonbusiness bad debt pursuant to Section 166(d) of the Internal Revenue Code of 1954 (26 U.S.C.), and that it was therefore deductible only as a short-term capital loss (Pet. App. 12-21).

The Tax Court also accepted the testimony of the Commissioner's expert witness that the value of the property on December 7, 1920, which provided the basis for determining the amount of petitioner's loss, was $85 per acre, rather than the $250 per acre urged by petitioner. Accordingly, it computed petitioner's loss to be $39,780 (Pet. App. 21-27). The court of appeals affirmed per curiam, on the basis of the Tax Court's opinion (Pet. App. 1-3).

1. The decision below correctly held that petitioner's loss on the foreclosure of the mortgage was deductible only as a short-term capital loss.

As both courts below found, petitioner was in substance a guarantor who became subrogated to the rights of the creditor upon payment of the guaranteed debt. In these circumstances, it is clear that any loss sustained by petitioner stems from the worthlessness of that debt in her hands. *Putnam* v. *Commissioner*, 352 U.S. 82, 88-89 (1956). Such a loss is subject to the provisions governing the deductibility of bad debts set forth in Section 166 of the Internal Revenue Code of 1954. Further, a bad debt loss is deductible as such or not at all. *Putnam* v. *Commissioner, supra.*[3] While bad debts proximately related

[3] Petitioner errs in her reliance (Pet. 3, 9-10, 16) on *Fox* v. *Commissioner*, 190 F.2d 101 (2d Cir. 1951), *Patterson* v. *United States*, 459 F.2d 487 (Ct. Cl. 1972), and *Mercer* v.

to the taxpayer's trade or business are deductible in full against ordinary income (Section 1.166-5(b), Treasury Regulations on Income Tax (26 C.F.R.)), a taxpayer is limited to short-term capital loss treatment for a nonbusiness bad debt under Section 166(d) of the Code. See *United States* v. *Generes*, 405 U.S. 93, 103 (1972).

Here, petitioner was a guarantor of the corporation's borrowing, to the extent that she pledged her property for its debts. There was, however, no evidence that she engaged in any trade or business, much less one that was proximately related to her guaranty of the corporation's debt. The corporation, not petitioner, pursued the trade or business of farming, and the business of a corporation is generally not imputed to that of its shareholders for purposes of taxation. *Whipple* v. *Commissioner*, 373 U.S. 193, 202-203 (1963); *Burnet* v. *Clark*, 287 U.S. 410, 415 (1932); *Dalton* v. *Bowers*, 287 U.S. 404, 410 (1932). Moreover, petitioner was not engaged in the trade or business of renting property; indeed, she neither executed any type of rental agreement with the corporation for the use of her property, nor collected even a nominal rent. See *Yanow* v. *Commissioner*, 44 T.C. 444 (1965), aff'd per curiam, 358 F.2d 743 (3d Cir. 1966). Accordingly, peti-

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Commissioner, 376 F.2d 708 (9th Cir. 1967), to support her contention that she suffered a loss under Section 165(c) of the Code. First, this Court in *Putnam* (352 U.S. at 93 n.21) expressly discredited, if it did not overrule, *Fox*. Further, neither *Patterson* nor *Mercer* involved a bad debt, and the holder of a bad debt, like petitioner, may not elect alternatively to claim an ordinary loss deduction under Section 165. See *Putnam* v. *Commissioner*, *supra*; *Spring City Co.* v. *Commissioner*, 292 U.S. 182, 189 (1934).

tioner's loss was a nonbusiness bad debt under Section 166(d) of the Code.[4]

3. The parties below treated petitioner's basis in the farm property transferred in satisfaction of the guaranty obligation as her basis in the debt. Moreover, it has been undisputed that the basis of petitioner's one-half interest in the farm property was derived from its fair market value on December 7, 1920, the date on which petitioner's mother acquired the property by gift from petitioner's father. See Sections 1015(a) and (c) of the Code.

Petitioner contends (Pet. 23-29) that the property was then worth $250 per acre and not $85 per acre, as determined by the Tax Court. But the Tax Court's factual determination (see *Commissioner* v. *Duberstein*, 363 U.S. 278, 291 (1960)) was based on the testimony of the Commissioner's expert witness, who carefully examined the sales of comparable farmland in the surrounding area between 1919 and 1922. Such a method of realty valuation has been widely upheld. See, *e.g.*, *Madison Gas & Electric Co.* v. *Commissioner*, 72 T.C. 521, 569 (1979), aff'd on another issue, 633 F.2d 512 (7th Cir. 1980). Petitioner's witnesses, on the other hand, lacked any expertise in assessing the value of real estate, and their opinions were not grounded on objective facts. Moreover, contrary to petitioner's suggestion (Pet. 23-24), the

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[4] *Schlumberger Technology Corp.* v. *United States*, 443 F.2d 1115 (5th Cir. 1971), *Trent* v. *United States*, 291 F.2d 669 (2d Cir. 1961), *Mays* v. *Commissioner*, 272 F.2d 788 (6th Cir. 1959), and *Giblin* v. *Commissioner*, 227 F.2d 692 (5th Cir. 1955), involving bad debts and upon which petitioner also relies (Pet. 19-22), are inapposite. In each of those cases, it was determined that the loans made were connected with the taxpayer's trade or business. Here, however, petitioner was not engaged in a trade or business.

Commissioner's expert witness properly excluded from his calculations the improvements situated on the property because they had been fully depreciated by the corporation prior to the year of the loss. See Section 1016(a)(2) of the Code. The Tax Court therefore correctly determined the value of petitioner's one-half interest in the property as of December 7, 1920.

It is therefore respectfully submitted that the petition for a writ of certiorari should be denied.

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Acting Solicitor General

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